CHERRYHILL RESOURCES INC.

1998 ANNUAL REPORT

TO THE SHAREHOLDERS

Cherryhill's first year of active operations proved to be a challenging one. In the fall of 1997, when the Company identified and pursued a property acquisition in Rocanville, Saskatchewan to be earmarked as its Major Transaction, oil prices averaged well above US $20/barrel (WTI). Conditions for raising capital for new production projects were favourable and Cherryhill's original expectation was that sound asset and financial growth would be readily achieved in 1998 through acquisitions supported by new equity injections and strong internal cash flow.

However, certain events unfolded in late 1997 and early 1998 that brought about a serious disruption in the world's oil market. An additional 2.5 million barrels per day of oil supply was added to the market as a result of overproduction by OPEC countries and the resurfacing of Iraq as a producer. This sudden surge in supply occurred when the world's consumption growth rate was declining due to the weakened Asian economies and an uncommonly temperate winter in North America. Any prospect of a near-term recovery continued to elude Asia and ongoing OPEC discussions failed to yield an agreement to curtail production levels from its more recalcitrant members. Consequently, the price of oil dropped steadily until it bottomed out at the US $11-12/barrel (WTI) range in late 1998.

Cherryhill completed its Major Transaction in April, 1998, at a period when the WTI price hovered around US $14-15/barrel. The Company acquired working interests in petroleum properties located in the Rocanville area of southeastern Saskatchewan that produced an estimated 40-45 barrels per day of light gravity oil. The consideration paid for the properties was $300,000. Despite the uncertainties facing the petroleum industry at the time, Cherryhill's management considered the Rocanville purchase to be a very worthwhile investment. The values assigned to the producing reserves by the Company's independent engineers as at January 1, 1998 were nearly twice as great as the cost of the assets (using both constant and escalated pricing and discounted at 15%), and therefore provided a buffer against further oil price declines. Furthermore, the area contained low-risk development potential, particularly within the recently-formed Rocanville Bakken Sand Voluntary Unit No. 2 (the "Unit"), of which Cherryhill acquired a 2.607% interest.

For the year ended December 31, 1998, Cherryhill generated sales revenue of $264,625. This represents ten months of production as the Major Transaction took effect on March 1, 1998. A net loss of $21,447, or $0.005 per share, was incurred for the period. Low commodity prices, workover and equipment repair expenditures of nearly $30,000, and non-recurring G&A and legal expenses associated with the Major Transaction were the primary factors that contributed to the loss. The Company's cash flow was $50,942, or $0.013 per share. Production averaged 46 barrels per day of oil during the ten months of active operations, and 48 barrels per day at year-end.

At December 31, 1998, the Company's land holdings in Rocanville spanned 4,680 gross acres (1,631 net acres) and consisted of operated and non-operated working interests ranging from 10-100% in six producing oil wells, two shut-in oil wells and the 2.607% non-operated Unit interest referred to above. The Unit was formed on November 1, 1997 and covers 1,400 gross acres of land within Sections 25, 26, 34, 35 and 36, Township 15, Range 31 W1M and Sections 2 and 3, Township 16, Range 31 W1M. A waterflood project was successfully completed in late 1997 in which four suspended or marginal oil wells were converted to water injectors. The Unit produces an average 730-740 barrels per day of oil (roughly 20 barrels per day net to Cherryhill) from 16 Bakken wells.

Cherryhill engaged in a number of acquisitions and drilling projects during the year that involved a small outlay of capital. It increased its working interest in three operated producing wells in Rocanville to 100% from 84% and acquired a 50% interest in a Crown lease near Weyburn, Saskatchewan. The Company also participated in drilling one oil well and a water injection well in the Unit, in addition to a Bakken oil well (10% BPO, 6% APO) adjacent to the Unit. Subsequent to the 1998 year-end, Cherryhill acquired, at a cost of $160,000, a 4.25% working interest in a property situated in Star Valley, Saskatchewan that produces an average 12 barrels per day of oil.

The recent recovery in the price of oil caused by dwindling world inventories and OPEC production cuts gives Cherryhill reason to be buoyant. An increase in the oil price will have an immediate impact on the company's earnings as operating costs are largely fixed. Furthermore, if current prices can be sustained throughout the year, and this will occur only if OPEC members can refrain from breaching their agreement, capital will be more readily available for new projects. The Company's short-term plans for the Rocanville properties are to engage in drilling additional wells in the Unit and possibly re-enter a non-Unit well, in which it holds a 40% working interest. Such projects can be financed internally and would moderately augment Cherryhill's production rate. Any meaningful or precipitous asset growth for the Company, however, would be achieved through acquisitions and require injections of new capital. Cherryhill is aggressively pursuing several opportunities involving the purchase of oil and natural gas properties in western Canada with quality reserves, steady income streams and development potential.

Cherryhill wishes to thank its outside directors for their wise counsel, and its shareholders for their continued interest and support.

Pauline Wong
President

April 15, 1999

AUDITORS' REPORT

TO THE SHAREHOLDERS OF
CHERRYHILL RESOURCES INC.:

We have audited the balance sheets of **Cherryhill Resources Inc.** as at December 31, 1998 and 1997 and the statements of income (loss) and retained earnings (deficit) and cash flow for the periods then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 1998 and 1997 and the results of its operations and cash flows for the periods then ended in accordance with generally accepted accounting principles.

Barr Shelley Stuart

CHARTERED ACCOUNTANTS

Calgary, Alberta
April 7, 1999

CHERRYHILL RESOURCES INC.

BALANCE SHEET
AS AT DECEMBER 31

			1998	1997
ASSETS				
CURRENT				
Cash		$	112,216	470,160
Accounts receivable			43,123	1,781
Prepaids			1,906	-
			157,245	471,941
PETROLEUM AND NATURAL GAS PROPERTIES	(Note 4)		300,741	-
		$	457,986	471,941
LIABILITIES				
CURRENT				
Accounts payable		$	16,873	22,805
PROVISION FOR SITE RESTORATION			13,424	-
			30,297	22,805
SHAREHOLDERS' EQUITY				
SHARE CAPITAL	(Note 5)		448,200	448,200
RETAINED EARNINGS (DEFICIT)			(20,511)	936
			427,689	449,136
		$	457,986	471,941

Approved on behalf of the Board:

_______________, Director
Richard A. Schuster

_______________, Director
John Komisar

CHERRYHILL RESOURCES INC.

STATEMENT OF INCOME (LOSS) AND RETAINED EARNINGS (DEFICIT)
FOR THE PERIODS ENDED DECEMBER 31

		1998	1997 (8 months)
REVENUE			
Oil and gas sales	$	264,625	-
Less royalties		(36,373)	-
		228,252	-
Interest income		9,270	4,580
		237,522	4,580
EXPENSES			
Oil and gas production		149,251	-
General and administrative		37,329	3,644
Site restoration		13,424	-
Depletion and amortization		58,965	-
		258,969	3,644
NET INCOME (LOSS) FOR THE YEAR		(21,447)	936
RETAINED EARNINGS AT BEGINNING OF YEAR		936	-
RETAINED EARNINGS (DEFICIT) AT END OF YEAR	$	(20,511)	936
LOSS PER SHARE	$	(0.005)	-

CHERRYHILL RESOURCES INC.

STATEMENT OF CASH FLOW
FOR THE PERIODS ENDED DECEMBER 31

	1998	1997 (8 months)
CASH PROVIDED BY (USED IN):		
OPERATING ACTIVITIES		
Net income (loss) for the year	$ (21,447)	936
Add items not involving cash		
Site restoration	13,424	-
Depletion and amortization	58,965	-
	50,942	936
Changes in working capital balances related to operating activities	(49,180)	21,024
	1,762	21,960
FINANCING ACTIVITIES		
Proceeds on issuance of shares	-	500,000
Share issuance costs	-	(51,800)
	-	448,200
INVESTING ACTIVITIES		
Purchase of petroleum and natural gas properties	(359,706)	-
INCREASE (DECREASE) IN CASH	(357,944)	470,160
CASH BEGINNING OF YEAR	470,160	-
CASH END OF YEAR	$ 112,216	470,160
CASH FLOW PER SHARE	$ 0.013	-

NOTE 1 INCORPORATION/NATURE OF BUSINESS

The Company was incorporated under the Business Corporations Act (Alberta) on May 8, 1997 and is engaged in oil and gas production and development.

NOTE 2 SIGNIFICANT ACCOUNTING POLICIES

These financial statements have been prepared by the Company's management in accordance with generally accepted accounting principles in Canada. In management's opinion, the financial statements have been properly prepared using careful judgement within reasonable limits of materiality and within the framework of the accounting policies summarized below:

Petroleum and Natural Gas Properties and Equipment

The Company follows the full cost method of accounting for petroleum and natural gas properties, whereby all costs associated with the exploration for, and the development of, petroleum and natural gas reserves whether productive or unproductive, are capitalized in cost centres. Costs capitalized include land acquisition costs, geological and geophysical expenditures, rentals on undeveloped properties and drilling and overhead expenses related to exploration and development activities. Proceeds from disposition of property sales are credited to the net book value of the property and equipment. Gains and losses are not recognized upon disposition of petroleum and national gas properties unless the disposition would significantly alter the rate of depletion.

Costs capitalized are depleted and amortized using the unit-of-production method based on net proved oil and gas reserves as determined by independent engineers. For purposes of the depletion calculation, proved oil and gas reserves are converted to a common unit of measure on the basis of their approximate relative energy content. The carrying value of undeveloped properties is excluded from the depletion calculation.

In applying the full cost method, the Company performs a ceiling test which restricts the capitalized costs less accumulated depletion, deferred income taxes and the site restoration provision from exceeding an amount equal to the estimated undiscounted value of future net revenues from proved oil and gas reserves, based on current prices and costs, and after deducting estimated future site restoration costs, general and administrative expenses, financing costs and income taxes.

NOTE 2 SIGNIFICANT ACCOUNTING POLICIES (Continued)

Estimated future site restoration costs are provided for on a unit-of-production basis over the useful life of the related reserves.

NOTE 3 MAJOR TRANSACTION

Cherryhill Resources Inc. was classified as a junior capital pool corporation (JCP) as defined in Alberta Securities Commission Policy 4.11. As its Major Transaction, completed on April 23, 1998, it purchased certain interests in petroleum properties situated in the Rocanville, Saskatchewan area from 599018 Alberta Inc. for a cash payment of $300,000.

599018 Alberta Inc., controlled by a director of the Company, purchased the Rocanville properties in an arm's length transaction on January 9, 1998 for a cost of $300,000.

NOTE 4 PETROLEUM AND NATURAL GAS PROPERTIES

	1998			1997
	Cost	Amortization & Depletion	Net Book Value	Net Book Value
Petroleum and natural gas properties	$ 359,706	(58,965)	300,741	-

NOTE 5 SHARE CAPITAL

Authorized
- Unlimited number of voting common shares
- Unlimited number of Class B preferred shares
- Unlimited number of Class C preferred shares
- Unlimited number of Class D preferred shares
- Unlimited number of Class E preferred shares

NOTE 5 SHARE CAPITAL (Continued)

Issued

	Number of Common Shares		Amount
Founders' shares	3,000,000	$	300,000
Public offering	1,000,000		200,000
Less share issuance costs	-		(51,800)
Balance December 31, 1998 and 1997	4,000,000	$	448,200

Under the requirements of the Alberta Securities Commission and The Alberta Stock Exchange, the 3,000,000 founders' shares are held in escrow and may be released upon written consent of the Alberta Securities Commission, as to one third thereof on the first anniversary of the completion of the Company's Major Transaction. At the time of consent for the first release, approval of the second and third anniversary releases may also be granted.

The preferred shares may be issued in one or more series and the directors are authorized to fix the number of shares in each series and to determine the designation, rights, privileges and conditions attached to the shares of each series.

The Company has adopted a Stock Option Plan for its directors and officers and has granted options which allow them to purchase 400,000 common shares at an exercise price of $0.20 per share. The options expire on June 5, 2002.

NOTE 6 INCOME TAXES

The Company has approximately $15,000 (1997 - $6,000) of non-capital losses which may be carried forward and applied against future income for income tax purposes. These losses begin to expire in 2003.

In addition, the Company will be able to claim future deductions for share issue costs totalling $36,036.

NOTE 7 RELATED PARTY TRANSACTIONS

During the year, a corporation controlled by a director was reimbursed for operating expenses paid on behalf of the Company. As of December 31, 1998, the Company had $2,862 due from this corporation. This amount has been received in full subsequent to year-end.

NOTE 8 MEASUREMENT UNCERTAINTY

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. Actual results could differ from those estimates.

NOTE 9 UNCERTAINTY DUE TO THE YEAR 2000 ISSUE

The Year 2000 Issue arises because many computerized systems use two digits rather than four to identify a year. Date-sensitive systems may recognize the year 2000 as 1900 or some other date, resulting in errors when information using year 2000 dates is processed. In addition, similar problems may arise in some systems which use certain dates in 1999 to represent something other than a date. The effects of the Year 2000 Issue may be experienced before, on, or after January 1, 2000, and, if not addressed, the impact on operations and financial reporting may range from minor errors to significant systems failure which could affect a company's ability to conduct normal business operations. It is not possible to be certain that all aspects of the Year 2000 Issue affecting the Company, including those related to the efforts of customers, suppliers, or other third parties, will be fully resolved.

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